IRS Oversight Board Annual Report

January 2002

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Executive Summary

In June 1997, the National Commission on Restructuring the Internal Revenue Service (IRS) set forth a vision for a new governance and management structure for the IRS. In July 1998, the IRS Restructuring and Reform Act of 1998 (RRA 98) enacted this vision through the creation of the IRS Oversight Board. Established in 2000, the Oversight Board has acted to assume its responsibilities and achieve the vision sought by Congress almost four years ago.

The Oversight Board has found that the IRS is still not effectively and efficiently serving the needs of the American taxpayers, although it has made significant progress since 1997. Customer service, although improved, has not risen to desired levels and enforcement activity has fallen for many years. These problems are compounded by outmoded computer systems that handicap IRS workers and prevent effective service from being delivered. It is not surprising that this environment has resulted in dissatisfied taxpayers and inadequate job satisfaction among IRS employees.

On the positive side, the IRS is making progress and has put in place several key elements that establish a foundation for further progress, including a Commissioner with a fixed term and a management background, a major reorganization designed to better focus on customer needs and provide clear accountability, a strengthened senior management team, and a business systems modernization program that will eventually provide modern business processes and tools for employees and taxpayers. The entire modernization effort is being conducted in accordance with a strategic plan that has been approved by the Oversight Board, and monitored by balanced performance measures that will provide Congress, the Administration, the Oversight Board and other stakeholders a quantitative means to evaluate progress.

To achieve its mission of "providing America's taxpayers top quality service by helping them understand and meet their tax responsibilities and by applying the tax law with integrity and fairness to all," the IRS has established these three strategic objectives:

- Service to each taxpayer
(customer service issues)
- Service to all taxpayers
(enforcement/compliance issues)
- Productivity in a quality workplace
(workforce/workplace issues)

Neither the IRS nor the Oversight Board is satisfied with the current state of IRS' performance. This report presents data that indicate the IRS needs to improve its performance in three dimensions: productivity, customer satisfaction, and employee satisfaction.

Performance measures for the key areas of customer service and enforcement were troubling to the Oversight Board. Customer service metrics pertaining to both level of service and quality associated with toll-free telephone operations need considerable improvement. Quality levels at IRS walk-in sites are just being baselined and need attention. Because of the link between employee and taxpayer satisfaction, employee satisfaction levels for these and other operations also need improvement.

Many factors influence IRS performance—among them staffing levels, tools, training, workforce productivity, tax code complexity, and management. There is little quantitative data that link the specific effect these or other factors have on various aspects of IRS performance. Many of the IRS performance problems can be attributed, at least in part, to increasing workload and a declining workforce over the last ten years, and its past inability to introduce major productivity gains through modernization.

The Oversight Board is concerned that the broad decline in enforcement activity increases our reliance on voluntary compliance, and fears that the public's attitude towards voluntary compliance is beginning to erode. Because of this concern, the Oversight Board initiated a survey to obtain data on taxpayers' attitudes regarding their obligations to report and pay their fair share of taxes. The survey, taken in August 2001, asked two questions from an earlier 1999 IRS survey and three new questions. **Table ES-1** depicts some key results from the survey.

The Oversight Board is reluctant to assign too much importance to a single survey, but notes that these results show a possible negative change in attitude relative to cheating on taxes. The Oversight Board intends to repeat the survey in 2002 using the same questions. There is cause for alarm if this trend continues.

To better understand compliance issues, the Oversight Board believes there is an urgent need for the IRS to increase its research on taxpayer compliance so it can identify and correct broad areas of taxpayer noncompliance. The IRS is developing a new program, the National Research Program (NRP), that will provide the necessary research. Past approaches were viewed by Congress and taxpayers as too intrusive, and the IRS is designing the NRP to lessen taxpayer burden while still obtaining a sample sufficient to produce meaningful results. The Oversight Board supports the NRP and requests Congressional support for this program.

Table ES-1: Key Survey Results

Question	1999	2001
How much, if any, do you think is an acceptable amount to cheat on your income taxes?		
• Not at all	87%	76%
Do you think it is more likely that people will not report and pay their fair amount of taxes now than in the past?		
• Yes, more likely	N/A	42%
Are you more inclined to take a chance of being audited now than you were in the past?		
• Yes, more inclined	N/A	9%

An effective IRS is an important part of our government, and the IRS can ill afford to fall behind. Old technology, a growing economy with more tax transactions, reduced IRS staffing levels, and an increasingly complex tax code have created a situation where the IRS must make up a lot of ground. This report presents data to better illustrate this point, but the Board believes that a private sector company that fell behind this dramatically would find its very survival threatened. However, we cannot allow the IRS to stagnate. Our society depends on a tax administration agency that can help taxpayers understand and meet their tax obligations and effectively enforce the tax laws.

The long-range solution to many of the IRS' problems is to modernize its business processes and information technology. The IRS' Business Systems Modernization (BSM) program is designed to transform both IRS' business processes and information technology into modern, efficient processes and systems that incorporate world-class best practices. The BSM program has been progressing slowly, limited primarily by IRS' capacity to manage the program. Efforts from inception to date have focused on establishing an enterprise life cycle, a standard architecture, and low-risk projects. In 2002, however, several major deliverables are scheduled, and the upcoming year will be a test of the IRS' ability to manage this program.

The longer it takes the IRS to modernize, the longer taxpayers will be deprived of the benefits of improved IRS processes and systems, and be forced to endure the inadequecies of antiquated systems in place today. Even under the best of circumstances, it will take the IRS far too long to complete its modernization program. The Oversight Board recommends that BSM be accomplished as quickly as possible, consistent with the IRS' ability to manage the program and absorb change. The private sector has already learned that accomplishing programs in as short a period as practical actually lessens overall cost and risk. To increase the pace of modernization, all organizations involved in BSM must do a better job. The Oversight Board's recommendations for key organizations include:

- The **IRS** must improve its program management ability, work more effectively with the PRIME Contractor, and manage/implement change more effectively.
- The **PRIME Contractor** must understand and achieve its responsibilities to deliver business results within budget and on schedule and improve its breadth and depth of skills.
- The **Administration** must understand the importance and critical nature of the situation, support the long term plan, including increased investment levels, and hold the IRS responsible for meeting the plan.
- The **Congress** must accomplish the same tasks as the Administration, and, in addition, speed up the process for review and release of BSM funding.
- **Oversight organizations** must rationalize their roles to the extent possible and eliminate unnecessary overlap, leverage assets to advise in a more effective manner; and recognize that quality cannot be achieved by repetitious, and at times, inefficient inspection.

Notwithstanding the need for a long-term modernization program, the IRS must also improve in the short term. Potential means of realizing short-term improvements may be organizational changes, process improvements, or modifications to the legacy technology base.

An IRS that performs better requires adequate funding as its workload continues to increase. As discussed in our interim report on the FY2002 budget, inadequate funding and resources will make it impossible for the IRS to meet any of its strategic objectives. The IRS still has a long way to go to reach the level of performance envisioned by both the IRS Restructuring Commission and the IRS Restructuring and Reform Act. Failure to provide adequate funding will deprive the IRS of resources it needs to make improvements in two major functions: customer service and compliance.

Current customer service levels are improving but still unacceptable. While technology and improved productivity can help improve performance, additional people and training are also required to enable the IRS to provide an acceptable level of service to taxpayers seeking assistance, both in person and over the telephone. Both activities are labor intensive and service levels are directly correlated to staffing levels.

Additionally, enforcement activity at the IRS has fallen while the volume and complexities of tax administration activities have increased. Voluntary compliance works if taxpayers believe the tax laws are being enforced equitably. Insufficient resources impede the IRS from improving enforcement efforts that ensure every taxpayer pays his or her fair share of taxes. It is unfair to burden the large majority of taxpayers who do comply with the tax laws by having them pick up the tab for those who do not. Fair and equitable enforcement is as much a service for honest taxpayers as providing them with assistance.

We strongly recommend that the Administration and Congress support the ongoing programs of improvement by providing adequate funding and support.

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I. Introduction

The IRS Oversight Board was established in September 2000, and has completed its first year of operation. The Internal Revenue Service Restructuring and Reform Act of 1998 (RRA 98) established the IRS Oversight Board to "oversee the IRS in its administration, management, conduct, direction, and supervision of the execution and application of the internal revenue laws or related statues and tax conventions to which the United States is a party." [1] The IRS Oversight Board has been given specific responsibilities to review and approve strategic plans of the IRS, review IRS operational functions, review the selection, evaluation, and compensation of IRS senior executives, and review and approve the budget request of the IRS prepared by the Commissioner.

The Oversight Board has acted to assume its responsibilities and achieve the vision sought by Congress almost four years ago. This report presents the activities of the Board during its first year of operation.

[1] RRA 98, Sec. 1101

2. Current State of the IRS

One of the first tasks undertaken by the IRS Oversight Board was to assess the current state of the IRS with respect to its mission. As previously reported,[2] the Board found that the IRS is not effectively and efficiently serving the needs of America's taxpayers. The Board identified the following pressing problems:

- Despite management focus and certain improvements, customer service is still not at a satisfactory level
- The level of enforcement activities has fallen consistently for many years, raising questions about tax compliance and fairness among the vast majority of citizens who pay their taxes
- The IRS computer systems are outdated, resulting in a work environment that is completely inconsistent with efficient and modern practices.
- IRS employee morale and job satisfaction are inadequate

Notwithstanding the severe problems the IRS is facing today, it has made significant progress in improving conditions since 1997. Some of its positive accomplishments include:

- A Commissioner with a management background and a five-year term was appointed and initiated sound business practices
- The IRS was reorganized into four major customer-focused divisions instead of geographical divisions, thereby creating greater concentration and accountability on taxpayer issues
- Additional taxpayer rights mandated by the RRA 98 were implemented
- The office of the Taxpayer Advocate was strengthened
- A technology modernization program was established to implement the business systems modernization program that is critical to future efficient and effective operations
- New executives with relevant private sector experience were recruited from outside the agency to improve its operations
- A five-year strategic plan, linked to the IRS budget, was developed by the IRS and approved by the Board

[2] IRS Oversight Board, *The IRS Budget Fiscal Year 2002, Analysis and Recommendations, Interim Report,* Spring 2001.

- Performance measures, encompassing business results, customer satisfaction, and employee satisfaction are being implemented

The IRS is currently in the midst of a massive modernization program, in which it is changing its organization, management personnel, business processes, measurement program, and technology. In conjunction with this modernization program, the IRS has established three strategic objectives, and is using performance measures to evaluate its progress in meeting these objectives:

- Service to each taxpayer (customer service issues)
- Service to all taxpayers (enforcement/compliance issues)
- Productivity in a quality workplace (workforce/workplace issues)

This report will summarize the current state of the IRS by presenting metrics for each of these objectives.

Service to each taxpayer

The IRS provides service to each taxpayer through a variety of services, primarily by assisting taxpayers understand their tax obligations, answering taxpayer questions using various channels, and processing paper and electronic returns.

Metrics for this objective assess the IRS' ability to deliver taxpayer service from both the IRS and taxpayer perspective, and include measures that evaluate the broad level of service that IRS provides through various customer service channels, the quality of those services, and taxpayer satisfaction levels with those services. **Table 1** provides selected metrics that relate to the quality and quantity of IRS services delivered to each taxpayer.

The metrics most troubling to the Oversight Board are the quantity and quality of services the

Table 1: Selected Metrics Assessing Service to Each Taxpayer

Metric	1999 Value	2000 Value	2001 Value
Toll Free Assistance			
Number of assistor calls answered (millions)	37.86	32.32	32.09 (Note 1)
Number of automated calls answered (millions)	60.77	49.70	76.12 (Note 2)
Level of Service (Note 3)	N/A	59%	56.4%
Quality of Service - Tax Law	74	73	75
Quality of Service - Accounts	82	60	69
Taxpayer Satisfaction	3.46	3.46	3.45
Walk-in Assistance			
Quality of Service (Note 4)	N/A	N/A	Baselining
Taxpayer Satisfaction (7-point scale)	6.43	6.48	6.40
Education and Outreach Staff Years	N/A	1,082	1,224
Web Site Hits (billions)	1.15	1.56	2.60
Returns Processed			
1040 Paper Returns (millions)	95.38	92.30	90.59
1040 Electronic Returns (millions)	29.32	35.37	40.22
Business Returns (paper)(millions)	79.69	81.59	83.15
Business Returns (electronic)(millions)	5.00	3.22	6.26
Roper Starch Favorability Rating	32	37	46
Agency-wide Employee Satisfaction	55%	59%	51%

Note 1: An estimated 3.3 million calls were related to the tax rebate program.
Note 2: An estimated 18.5 million calls were related to the tax rebate program.
Note 3: Definition changed from 1999 to 2000 to reflect more precisely the kind of servide provided by assistors.
Note 4: A preliminary analysis by TIGTA raised serious questions about the quality of service at IRS walk-in sites. The IRS is now implementing a standard methodology to assess quality at these sites.

IRS provides to taxpayers through toll-free telephone assistance and walk-in sites. The decline in agency-wide employee satisfaction is also troubling, and requires corrective action and monitoring. Admittedly service is hampered by the lack of modern tools and technology for providing better service. Although the IRS needs to pursue these types of solutions, it must be recognized that there is a direct correlation between the number of calls that can be answered and staffing levels. Approaches must be developed that allow the IRS to develop a better understanding of the interrelationship needed to improve these services. Approaches for improving customer service should include analysis of balanced measures such as employee and customer satisfaction.

Under its new organization, the IRS is emphasizing taxpayer education and outreach and has created organizational units dedicated to providing more of this type of service to both individual taxpayers and small businesses. This approach is based on the premise that these services will improve voluntary compliance and reduce taxpayer burden. Table 1 shows that resources are increasing for these services, but approaches must be developed to assess quantitatively the long-term results that these efforts are intended to produce.

The most dramatic change indicated in Table 1 is the Roper Starch Favorability Rating, which measures overall taxpayer satisfaction with the IRS. While still not at a level that we would like to see, this survey shows a 44 percent improvement in the last two years. This is a clear indication that IRS improvement programs are having an impact.

Service to all taxpayers

The IRS provides service to all taxpayers by ensuring that tax laws are administered fairly for all taxpayers. Metrics for this objective assess the IRS' ability to ensure all taxpayers are reporting and paying their fair share of taxes and enforcement is equitable across all segments of the taxpayer population, while protecting the rights of individual taxpayers.

Tax enforcement results were on a uniformly steady decline from 1996 through 2001, as shown in **Table 2**.[3] Results for 2000 and 2001 are mixed, but do indicate a small upward trend for many measures. One exception is the number of audits, which generally continue to decline uniformly, except for correspondence audits of taxpayers with income in excess of $100,000. In any case, major improvement is still needed. Resources for enforcement functions have declined during the same period, but at a lesser rate.

Other factors that may have contributed to the decline in enforcement results are changes in Section 1203 of RRA 98 that mandate termination of IRS employees for misconduct and ineffective use of measures to monitor organizational performance. No data exist that can validate the actual causes for the decline, although the General Accounting Office (GAO) has started such a study.

The Board has evaluated the benefits of changes to Section 1203 and has corresponded with the Chairman and Ranking Member of the Senate Finance Committee supporting changes to Section 1203 of the RRA 98. Although the Board did not endorse a particular legislative solution, it did identify the following four guidelines that it believed could form the basis of needed reform of Section 1203:

1. The mandatory termination punishment should be eliminated to provide discretion for IRS management.

2. "Willfulness" should be an element in any offense under this section.

3. An employee's failure to file his or her tax return should not be an automatic removal offense when the employee is due a refund.

4. Employee versus employee allegations

[3] Treasury Inspector General for Tax Administration (TIGTA) Report 2000-30-075, Dated May 2000, updated for 2000.

Table 2: Six Year Trend in Enforcement Metrics

Enforcement Metrics	1996	1997	1998	1999	2000	2001
Enforcement revenue collected ($ billions)	38	37.2	35.2	32.9	33.8	33.8
Gross accounts receivable ($ billions)	216.3	236.1	246.1	257.2	264.4	275.9
Unpaid accounts in the "queue"	754,983	993,121	933,715	1,197,963	1,532,682	1,722,662
Number of unfiled return investigations	326,118	435,337	456,711	1,282,919	1,876,629	821,188
Delinquent accounts closed						(Note 1)
by Revenue Officers (ROs)	1,703,629	1,680,328	1,331,964	1,037.919	977,338	810,832
by ROs with full payment	481,409	494,567	398,718	275,981	235,797	239,503
by Automated Collection Systems (ACS)	3,129,998	3,201,929	2,823,373	2,554,099	3,234,328	2,888,453
by ACS with full payment	901,145	893,620	793,958	688,622	679,872	742, 563
Federal tax liens filed	750,225	543,613	382,755	167,867	287,517	428.376
Levies served	3,108,926	3,659,417	2,503,409	504,403	219,778	447,201
Seizures made	10,449	10,090	2,307	161	174	255
Individual returns under $100,000 audited by correspondence	1,260,145	922,109	742,335	778,932	395,200	(Note 2)
Individual returns under $100,000 audited face-to-face	470,487	396,381	285,484	192,231	122,497	(Note 2)
Individual returns over $100,000 audited by correspondence	84,008	68,065	53,026	43,294	44,393	(Note 2)
Individual returns over $100,000 audited face-to-face	125,253	131,128	110,873	84,799	54,932	(Note 2)
Corporate income tax returns audited (< $5M assets)	42,836	51,870	37,915	25,285	16,566	(Note 2)
Corporate income tax returns audited (> $5M assets)	16,508	17,348	15,647	13,459	11,221	(Note 2)

Note 1: During 2001, 1,269,959 investigations were closed administratively without taking any action.
Note 2: Data for 2001 were not available at the time this report was prepared.

should not be a part of section 1203.

In addition to the results-oriented metrics shown in Table 2, other metrics assess the quality of the transactions involving service to all taxpayers through enforcement, such as taxpayer satisfaction with the process and quality of the result. **Table 3** provides selected data relevant to these considerations.

These results are mixed. Taxpayer satisfaction has generally increased, but productivity and quality metrics have either declined or failed to improve significantly. These results have been achieved in

Table 3: Selected Metrics Assesing Services to All Taxpayers

Metric	1999 Value	2000 Value	2001 Value
Collection activity by telephone and correspondence			
Taxpayer satisfaction (4 point scale)	3.32	3.41	3.46
Delinquent investigations closed	909,303	729,410	297,791
Telephone Level of Service	81%	79%	77%
In-Person collection activity			
Customer satisfaction (seven point scale)	3.89	4.45	5.01
Delinquent investigations closed	166,808	144,764	119,451
Offers in Compromise processed	49,051	69,514	97,013
Document matching cases closed	3,367,086	2,888,900	2.511,424
Document matching case quality score	N/A	93%	95%
Examination customer satisfaction			
By telephone and correspondence (7 point scale)	3.87	4.04	4.18
In-person examination (7 point scale)	4.08	4.41	4.65
Examination case quality			
By telephone and correspondence	91%	70%	71%
In-person examination	65%	58%	70%

an environment where resources have declined and the organization is undergoing major changes. There are signs that the organizational situation is becoming more stable as the new organization matures, and 2002 is expected to bring an improvement in performance levels. The Board will monitor these measures closely to determine what improvement actually occurs.

Taxpayers' attitudes regarding the fairness of the tax administration system and their obligations to report and pay their fair share of tax are important measures that impact voluntary compliance. The Oversight Board initiated a survey to obtain data on taxpayers' attitudes regarding their tax obligations. The Oversight Board was concerned that the public's attitude towards voluntary compliance was beginning to erode, especially after a major media report that questioned whether taxpayers should report honestly.[4]

The survey was conducted in August 2001 and was composed of five questions. The first two questions were identical to questions asked in a similar IRS survey in 1999 to obtain some longitudinal data on changes in attitude. The other three questions were used for the first time, and attempted to measure if taxpayers believed that more of their fellow citizens were not complying with the tax code. **Table 4** contains a summary of the data obtained from the survey.

Table 4: Summary of Survey Results on Taxpayer Attitudes

	1999	2001
Question 1		
How much, if any, do you think is an acceptable amount to cheat on your income taxes?		
Not at all	87%	76%
A little here and there	8%	11%
As much as possible	3%	5%
Don't know/not sure	2%	8%
Question 2	**Agree**	**Agree**
Level of agreement with statement		
It is every American's civic duty to pay their fair share of taxes	96%	91%
Everyone who cheats on their taxes should be held accountable	89%	80%
It is everyone's personal responsibility to report anyone who cheats on their taxes	48%	34%
Taxpayers should just have to pay what they feel is a fair amount	26%	28%
Question 3		
Do you think it is more likely that people will not report and pay their fair amount of taxes now than in the past?		
Yes, more likely	N/A	42%
No, not	N/A	32%
Don't know	N/A	26%
Question 4		
Do you think it is more likely that people who do not report and pay their fair share of taxes will be audited now than in the past?		
Yes, more likely	N/A	33%
No, not	N/A	37%
Don't know	N/A	30%
Question 5		
Are you more inclined to take a chance of being audited now than you were in the past?		
Yes, more inclined	N/A	9%
No, not	N/A	76%
Don't know	N/A	15%

[4] Janet Novack, "Are You a Chump?", Forbes Magazine, March 5, 2001, page 122.

The Oversight Board is reluctant to assign too much importance to a single survey, but does note that the response to question one shows a possible negative change in attitude on cheating on taxes. In 1999, 87 percent of responders said it was not acceptable at all to cheat on taxes, but in 2001 that number had fallen to 76 percent. In addition, over 40 percent of taxpayers believe that it is more likely that their fellow taxpayers are not reporting and paying their fair share of taxes now than in the past.

The Oversight Board intends to repeat the survey in 2002 using the same five questions. As more surveys are conducted, a picture will emerge of any shift in taxpayer attitudes. There is cause for alarm if this trend continues.

The Oversight Board also believes there is an urgent need for the IRS to increase its research on taxpayer compliance so it can identify and correct broad areas of taxpayer noncompliance. The IRS discontinued its Taxpayer Compliance Measurement Program (TCMP) in 1995 amid complaints that it was too intrusive. As the problems caused by the lack of research are now becoming more apparent, the IRS is starting to develop the National Research Program (NRP) that will collect the necessary research data. The IRS is designing the NRP to lessen taxpayer burden while still obtaining a sample sufficient to produce meaningful results. The Oversight Board supports the NRP and requests Congressional support for this program.

Productivity in a quality workplace

Because RRA 98 prohibited the use of tax results to evaluate individual IRS employees, in 1998 the IRS discontinued the use of measures to evaluate individual productivity. Subsequently, the IRS developed a balanced measures program and has begun to implement this program from the enterprise level down to the unit level. Although certain productivity measures may not be used to evaluate the performance of individual employees, the IRS does not collect enterprise-wide metrics that relate to productivity. **Table 5** presents selected metrics that are relevant to assessing productivity in a quality workplace.

Many, but not all, measures of IRS productivity have decreased during the past three years. It is not clear why this decrease in productivity has occurred. Only by analyzing all data—business results, quality, customer satisfaction, and employee satisfaction—in a balanced way can a true picture be developed. The Board expects that the IRS will use balanced measures data to develop performance improvements during 2002 with an objective of using this data to drive real gains in performance. The Board will monitor IRS' performance to assess results, both by organizational element and individual executives.

There may be a variety of possible reasons for the changes in the measures presented in Table 5. Some explanation may be found in declining resource allocations, but other reasons relate to low employee satisfaction, additional case complexity, less direct time spent on cases, and additional legislated requirements.

The IRS contracted with the Gallup Organization to survey its employees to measure their level of engagement. The objectives of the survey were to understand the dimensions of employee engagement at the IRS that consistently drive business outcomes. The results were to act as benchmarks of workplace quality versus those of other organizations; to learn about workplace strengths; to review opportunities for improvement; and to analyze the factors that drive the IRS' workplace culture. Find-

Table 5: Selected Metrics Assessing Productivity in a Quality Workplace

Metric	1999 Value	2000 Value	2001 Value
Total toll-free calls answered by assistors (Wage & Investment [W&I] only) (millions)	N/A	18.4	18.3
Toll-free calls per productive unit of effort	4,381	3,897	3,868
Tax Assistance Centers Total Walk-in contacts	9,980,959	9,663,065	9,681,330
Innocent Spouse determinations made and claimant notified (Note 1)	27,936	55,698	61,011
Number of products developed (small business workshops)	N/A	334	1,181
Number of Offers-in-Compromises (OIC) processed (SB/SE)	49,051	69,514	97,013
Offer-in-Compromise ending inventory (Note 2)	N/A	87,456	94,941
Automated Underreporter (AUR) closures	3,367,086	2,888,900	2,511,424
Large- and Mid-Size Business (LMSB) prefiling agreements	N/A	6	5
Cases closed-coordinated industry (LMSB)	416	328	417
Exempt Organization (EO) determination cases closed	74,603	81,395	79,854
EO examinations closed	8,519	7,237	5,342
Number of taxpayer advocacy projects	N/A	88	92
Taxpayer Advocate Service (TAS) regular criteria closed case cycle time	46.1	53.7	72.3
TAS open inventory (regular criteria cases)	33,726	53,475	59,647
Number of criminal investigations completed	4,263	3,499	3,340
Appeals-total consolidated non-docketed case cycle time	223	222	224
Appeals-total disposals	61,507	54,986	54,748

Note 1: Innocent spouse tracking commenced on March 6, 1999 as a result of additional relief for innocent spouses provided by RRA 98. The National Taxpayer Advocate has reported that due to the large influx of cases, process timeframes are not always met, but the IRS has taken positive steps to improve innocent spouse claim processing.

Note 2: The National Taxpayer Advocate has reported a large rise in Offer-in Compromise applications and processing delays caused by the IRS' ability to keep pace with the growth.

ings from that survey indicate that the lack of engagement among some employees at the IRS is negatively affecting its ability to achieve its mission. Key weaknesses the IRS must overcome include a lack of a sense of mission, lack of recognition, and increased engagement from front line employees. These are serious challenges that will take a concerted effort to overcome.

The IRS must gather data to determine the root causes for the decline in productivity measures. The Oversight Board believes it is critical that the IRS make better use of existing data to analyze potential problems and apply corrective action.

3. How Did the IRS Get in This State

The current state of the IRS did not happen overnight, nor was it the result of a single cause or factor. Failure to keep pace with technology is one, but not the only, cause. The lack of a customer service attitude toward taxpayers is another one. In a larger sense, the IRS became stagnant and failed to improve with the times. Acceptable processes, systems, and culture from the 1960s and 1970s failed to keep pace with a society that evolved from rigid models of customer service and centralized, tape-sequential data systems to modern models of real or near-real time data systems accessible electronically directly by the customer on a round-the-clock basis.

The state of IRS technology is rooted in the 1960s. When this technology was developed, life was far simpler and slower-paced than today. Banking was done in person with a teller, not an ATM. Homes had rotary dial telephones and long distance service was a luxury. Credit cards were scarce and paper checks common. Computers were bulky and found only in environmentally controlled spaces, never in homes or offices. Correspondence was prepared using typewriters.

The Information Age transformed life in the 21st century. Computers are everywhere, including the home. Telephone usage has grown beyond all expectations. Many financial services are available on a 24x7 basis through electronic media. Data and e-commerce services are available through the Internet to satisfy our insatiable need for information. Although Americans wrote 66 billion checks in 1997, credit cards are common and financial institutions are always working to squeeze every day of float out of financial transaction systems.

The IRS master files, designed in the 1960s with a weekly update cycle, were appropriate for their time. Unfortunately, the IRS is still using these systems today, even as the world has changed around it in the last 40 years. The fact that these systems are still working is a tribute to the skilled workers at the IRS, many of whom are approaching retirement age. However, many critics claim that IRS legacy systems are living on borrowed time.

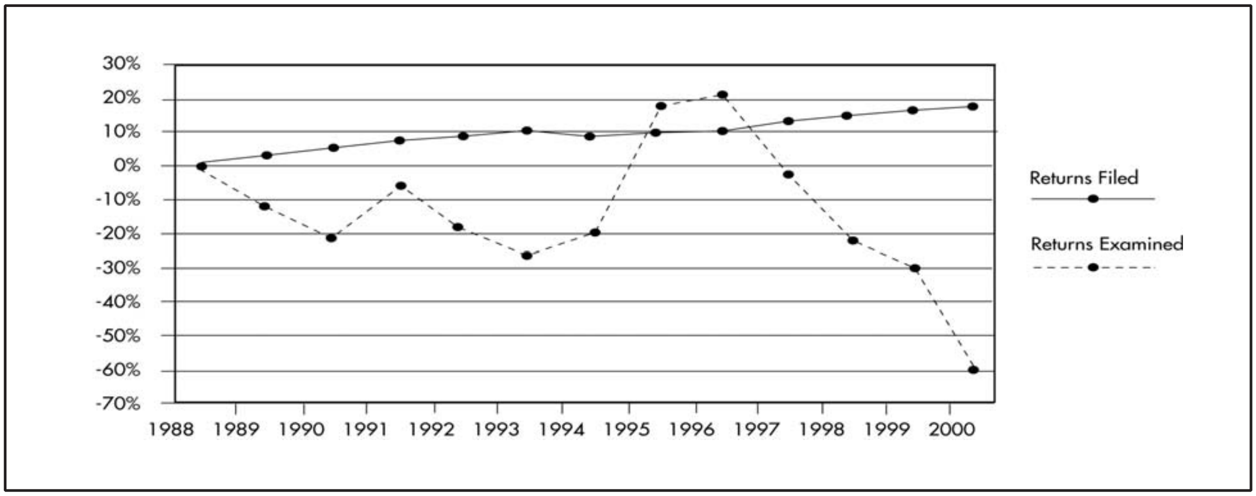
The purpose of this report is not to assign blame; rather, it is to point out that the IRS must make up a lot of ground. A private sector company that fell behind this dramatically would find its very survival threatened. However, our society depends on a tax administration agency that can help taxpayers understand and meet their tax obligations and effectively enforce the tax laws. We cannot allow the IRS to continue to stagnate.

Three other factors have exacerbated the problem during the last decade—a growing economy, reduced staffing level at the IRS, and an increasingly complex Internal Revenue Code. During the last ten years, the amount of revenue collected by the IRS has grown from $1.06 trillion in 1990 to $2.1 trillion in 2000. This growth has also been characterized both by an increased number of transactions and increased transaction complexity. Several examples are provided below to illustrate this point.

From 1988 to 2000, the total number of tax returns filed **increased** by 18 percent (from 140.33 to 165.77 million). During the same time period, the number of tax returns examined **decreased** by 60 percent (from 1.77 million to 715,915). (See **Figure 1**) Taking both statistics into account, the number of tax returns examined went from one out of every 79 in 1988 to one out of every 232 in 2000.

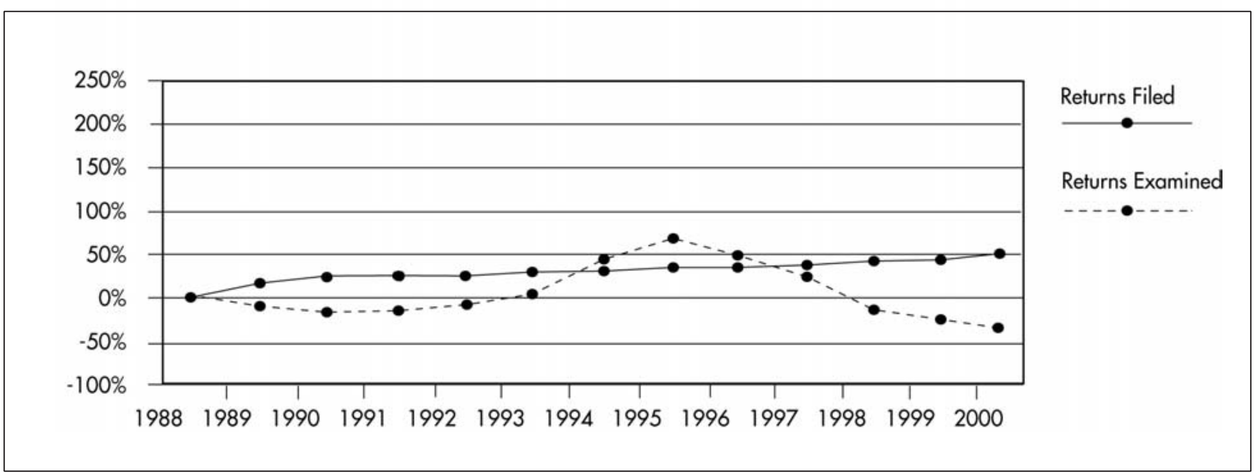
While these statistics do not recognize the significant amount of tax return data that is compared to independent sources such as W-2s and 1099s, the Board believes that the statistics represent a very real and troubling trend in enforcement activity.

Figure 1: Examination Coverage of All Returns Filed — Percentage Change From 1988



Source: TIGTA Report 2001-30-175, Tax Return Filing and Examination Statistics

Figure 2: Examination Coverage of Individual Tax Returns With Primarily Business Income (Excluding Farms)— Percentage Change From 1988



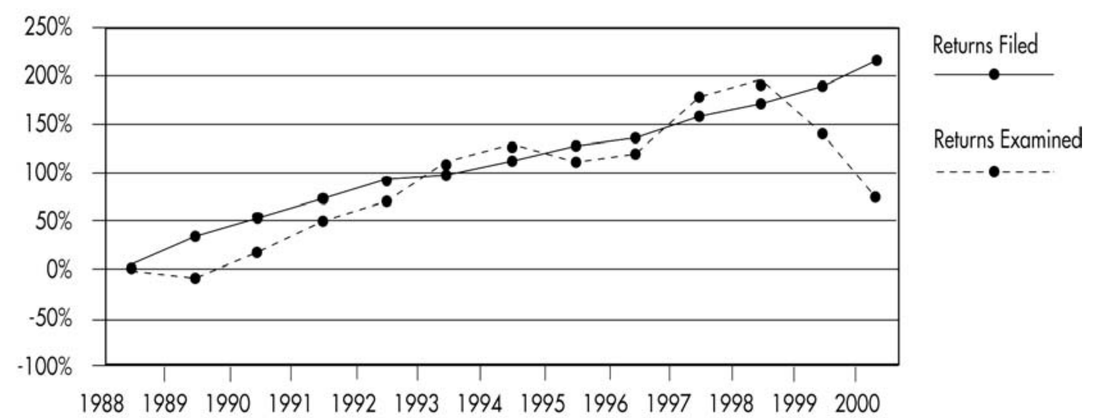
Source: TIGTA Report 2001-30-175, Tax Return Filing and Examination Statistics

The number of business individual tax returns (individual tax returns that contain primarily business income as reported on a Schedule C) filed **increased** by 48 percent (from 5.30 to 7.84 million), while the number examined **decreased** by 32 percent (from 178,076 to 121,702). (**Figure 2**)

The number of S Corporation tax returns filed increased by 210 percent (from 892,000 to 2.77 million), and the number examined increased by 74 percent (from 8,757 to 15,200). While the number of examinations kept pace with the number of returns filed through 1998, the number decreased significantly in 1999 and 2000. (**Figure 3**)

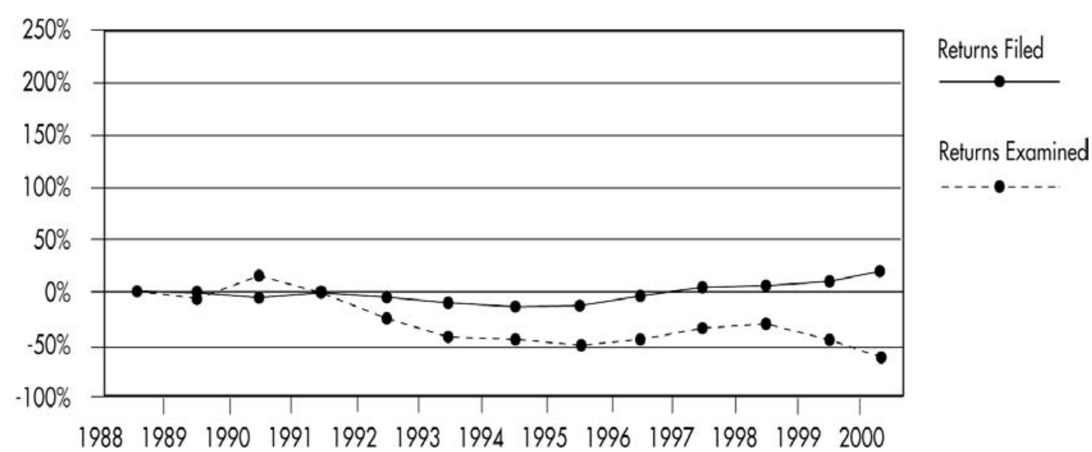
The number of partnership tax returns filed increased by 16 percent (from 1.70 to 1.97 million) from 1988 to 2000. On the other hand, the number of these tax returns examined decreased by 55 percent (from 14,652 to 6,539). (**Figure 4**)

Figure 3: Examination Coverage of S Corporations Tax Returns — Percentage Change From 1988



Source: TIGTA Report 2001-30-175, Tax Return Filing and Examination Statistics

Figure 4: Examination Coverage of Partnership Tax Returns — Percentage Change From 1988

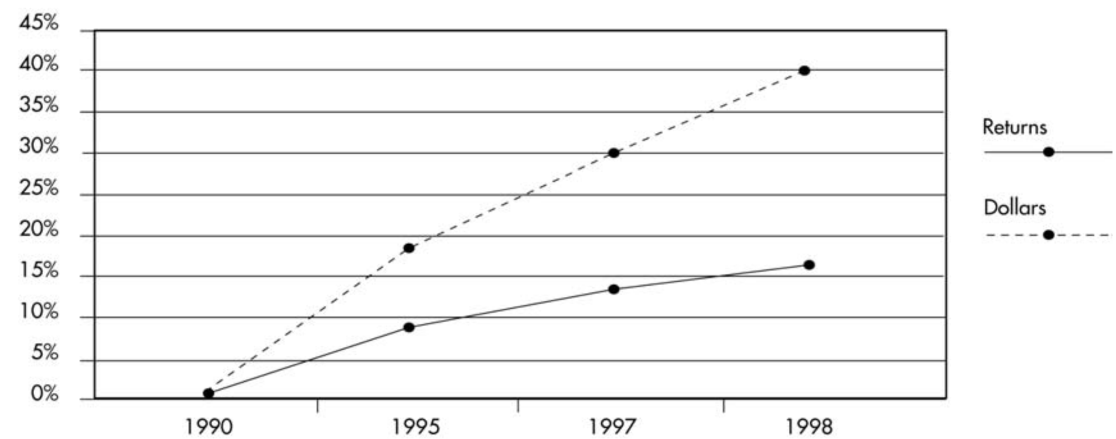


Source: TIGTA Report 2001-30-175, Tax Return Filing and Examination Statistics

The number of individual income tax returns filed that included business or profession net income **increased** by 17 percent (from 11.22 to 13.08 million). The income **increased** by 40 percent (from $161.66 to $226.14 billion). (Figure 5)

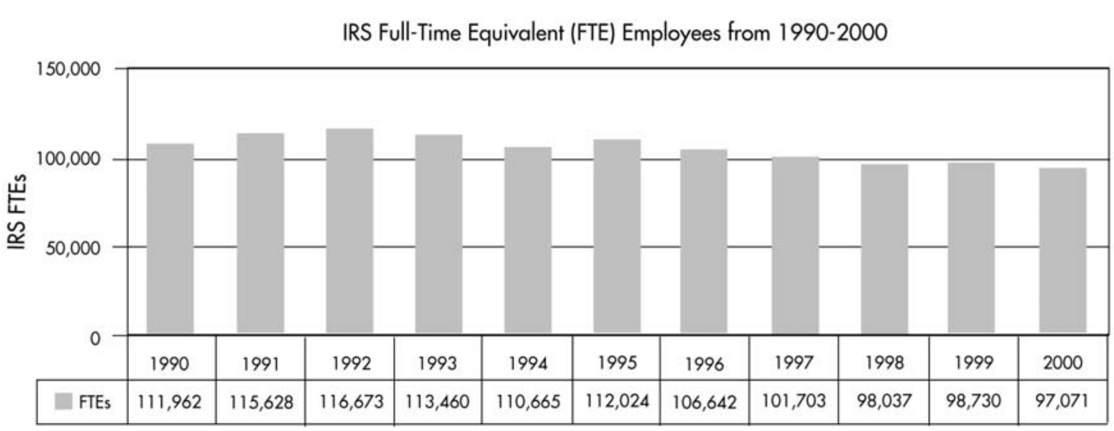
While tax transactions were growing, as noted above, the number of IRS employees was shrinking. From 1990 to 2000, the number of full-time equivalent (FTE) employees at the IRS went from 111,962 to 97,071, as illustrated in Figure 6. Unfortunately, the Tax Systems Modernization (TSM) program, which was started in the early 1990s to modernize IRS systems, failed and had to be terminated. Had TSM been successful, increased efficiencies would have compensated for decline in employees, but the failure of TSM left the IRS dependent on its old systems and their inherent weaknesses.

Figure 5: Indivdual Returns With Business or Professional Net Income Percent Change From Tax Year 1990



Source: TIGTA Report 2001-30-175, Tax Return Filing and Examination Statistics

Figure 6: Changes in Number of IRS Employees from 1990-2000



	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000
FTEs	111,962	115,628	116,673	113,460	110,665	112,024	106,642	101,703	98,037	98,730	97,071

Source: IRS Data Book 2000

Concurrent with the economic growth and loss of employees, the Internal Revenue Code was becoming increasingly complex. An April 2001 tax simplification study conducted by the Joint Committee on Taxation reported the following characteristics of the Internal Revenue Code[5]:

- The Internal Revenue Code consists of approximately 1,395,000 words;

- There are 693 sections of the Internal Revenue Code that are applicable to individual taxpayers, 1,501 sections applicable to businesses, and 445 sections applicable to tax-exempt organizations, employee plans, and governments;

- As of June 2000, the Treasury Department had issued almost 20,000 pages of regulations containing over 8 million words;

- During 2000, the IRS published guidance for taxpayers in the form of 58 revenue rulings, 49 revenue procedures, 64 notices, 100 announcements, at least 2,400 private letter rulings and technical advice memoranda, 10 actions on decision, and 240 field service advice;

- For 1999, publications of the IRS included 649 forms, schedules, and separate instructions totaling more than 16,000 lines, 159 worksheets contained in IRS instructions to forms, and approximately 340 publications totaling more than 13,000 pages;

- A taxpayer filing an individual income tax return could be faced with a return (Form 1040) with 79 lines, 144 pages of instructions, 11 schedules totaling 443 lines (including instructions), 19 separate worksheets embedded in the instructions, and the possibility of filing numerous other forms (IRS Publication 17, Your Federal Income Tax [273 pages], lists 18 commonly used forms other than Form 1040 and its schedules);

- In 1997, of the more than 122 million individual income tax returns filed, nearly 69 million were filed on Form 1040, as opposed to Form 1040A, Form 1040EZ, or Form 1040PC;

- In 1999, taxpayers contacted the IRS for assistance approximately 117 million times, up from 105 million contacts in 1996; and

- The use of paid return preparers increased from 48 percent of returns filed in 1990 to 55 percent of returns filed in 1999 and the use of computer software for return preparation increased from 16 percent of returns filed in 1990 to 46 percent of returns filed in 1999.

The IRS Oversight Board is precluded by the RRA 98 from becoming involved in specific tax policy. However, the January 2002 report of the National Taypayer Advocate states that tax code complexity increased administrative burden for both taxpayers and the IRS. The Oversight Board is of similar belief and strongly supports simplification of the tax code.

[5]Study of the Overall State of the Federal Tax System and recommendations for Simplification, Pursuant to Section 8022(3)(B) of the Internal Revenue Code of 1896, Volume 1: Study of the Overall Study of the Overall State of the Federal Taxation System, April 2001, page 4.

4. The IRS Must be Fixed

As demonstrated by the data presented, the IRS faces many challenges that must be overcome if the IRS is to improve its operations. Among the myriad challenges faced by the IRS, the most serious include the following:

- The state of IRS technology
- Service levels to taxpayers
- Declining results in enforcement
- Lack of compliance data to make informed resource allocation decisions
- Declining productivity
- Workforce engagement
- Rolling out the balanced measures program
- Ability to manage change
- Ability to modernize
- Human capital challenges

The IRS must upgrade its basic technology to deliver services in modern times. Weekly posting of account data must give way to daily or on-line posting. Electronic transactions need to become commonplace. The biggest impediment that prevents the IRS from this vision is its anachronistic master files, large files of tax information stored on computer tapes that are only updated once a week. This system prevents taxpayers from receiving up-to-date account information and creates chaos with both taxpayers and IRS representatives, and, worse yet, until it is replaced, inhibits meaningful progress on IRS modernization.

The anachronistic computer systems in use at the IRS have also impacted the services it provides to taxpayers, who have become accustomed to far better service from private sector financial institutions. Electronic transactions, real-time posting, responsive telephone service, and one-call resolution of issues are all characteristics of modern financial institutions. The IRS must offer this type of world-class service to taxpayers.

As shown in Table 2, virtually all measures of enforcement results have declined in the past five years, which increases our reliance on voluntary compliance. Reversing this trend in declining enforcement must be a high priority of the IRS. Improvement in compliance results must be driven by use of more systemic and efficient approaches to enforcement. Developing such approaches will be aided by better research that can identify areas of noncompliance and allow for more systemic enforcement.

The IRS has reorganized into four primary customer-facing divisions instead of the geographical organizational units that had been in place since

1952. As part of this reorganization, managers had to compete for new positions. Although this new organization seems to hold promise for future efficiencies, the impact of this massive organizational change is still being felt in the IRS.

Managing change in organizations large or small is never easy, but the organization change currently being implemented at the IRS is only the beginning of a series of major changes. Changes that will be implemented in the future include changes to the IRS' measurement systems, business processes, and technology systems. The ability to manage change will be a major challenge for the IRS over the next decade. The benefit received from new processes and information systems will never be fully realized until they are fully absorbed within the IRS culture as a new way of doing business.

The IRS, like many federal agencies, has an aging workforce. Many of its older workers have key roles in maintaining systems that have been in place for decades. Also, among senior executive ranks, key executives are already eligible to retire and could do so in the near future. An exodus of human capital without trained replacements can have a severe impact on IRS operations, and lead to even lower quality, productivity and satisfaction rates in the future. Careful planning and identification of replacements for key individuals should not be left until a crisis occurs. Thoughtful approaches to resolve these critical human capital issues are needed in the next year to avert a future crisis.

5. Progress is Being Made

The IRS began its current business systems modernization program in 1997 with the publication of the Modernization Blueprint, which established an architectural framework. With the appointment of Charles Rossotti as IRS Commissioner in 1997, the program was expanded into a comprehensive overhaul of the entire agency using the following five levers of change:

- Organization
- Workforce/Skills
- Measures
- Processes
- Technology

The IRS has modernized its organization into four primary divisions that each provide service to four separate groups of taxpayers. This reorganization has been the largest change in the IRS' organization since 1952. It was put in place in October 2000, but some elements are still being implemented. An employee survey conducted by the Gallup Organization in 2001 verified there are still issues the IRS must address to fully engage the workforce in the new organization.

The IRS received new personnel flexibilities in RRA 98 to hire senior executives at higher rates of pay than other civil service positions. This authority, know as streamlined critical pay, has allowed the IRS to hire a cadre of outside executives into the agency in various positions. However, the IRS has not hired all the critical pay executives it has been authorized, and in key areas such as information technology management, hiring additional outside executives to bolster the current team would benefit the IRS. The Oversight Board has recommended that the IRS modify its hiring process for streamlined critical pay positions to include an analysis, for each offer, of the critical skills needed by IRS, how the proposed candidate fulfills those needs, and the shortage of those skills in the marketplace that justify classifying them as critical and qualifying for higher compensation.

In 2002, the IRS will complete the implementation of its new balanced measures program throughout the organization. Prior to RRA 98, the IRS had focused its measures on business results. As a result of RRA 98, it stopped the use of measures until it could roll out a balanced measures program. The balanced measures program combines business productivity measures with quality, customer satisfaction, and employee satisfaction measures.

The success of the balanced measures program will not come from just acquiring additional or better data on conditions at the IRS. The data collected must be analyzed to evaluate progress and used to design performance improvement efforts that eliminate problem areas and foster further improvement. Learning from the data collected and using it to drive improvement is an organizational skill that the IRS must develop to a far greater extent than it has to date.

The IRS' Business Systems Modernization (BSM) program is designed to transform both IRS' business processes and information technology into modern, efficient processes and systems that incorporate world-class best practices. The BSM program has been progressing slowly, limited primarily by the IRS' capacity to manage the program. Efforts from inception to date have focused on establishing an enterprise life cycle, a standard architecture, and low-risk projects. In 2002 however, several major deliverables are scheduled, and the upcoming year will be a test of IRS' ability to manage this program.

The year 2002 will be a critical year for the IRS. The Operating Divisions are entering their second year of operation, and are expected to overcome the transition problems experienced last year. Balanced measures will assist management to evaluate the state of IRS operations. New leadership is in place at the position of Deputy Commissioner for Modernization, and the IRS is expected to achieve improved capability to manage the BSM program and deliver key products.

6. Board Recommendations on IRS Modernization Program

For the IRS to transform itself into a modern financial institution, all five levers of change must succeed. Managing change will be a major challenge for the IRS in the next five to ten years. The IRS must make the ability to respond to change a part of its culture.

The longer it takes to modernize, the longer taxpayers will be deprived of the benefits of improved IRS processes and systems, and be forced to endure the inadequacies of antiquated systems in place today. Even under the best of circumstances, it will take the IRS far too long to complete its modernization program, at least ten years. For these reasons, the Oversight Board recommends that BSM be accomplished as quickly as possible, consistent with the IRS' ability to manage the program and absorb change. The private sector has already learned that accomplishing programs' in as short a period as practical actually lowers cost and risk.

The BSM program is a major investment and will require significant ongoing and growing multi-year funding. Although current funding levels have been limited by the IRS' ability to manage the program, the funding level must increase as the IRS gets further into the program. This means the IRS must continue to increase its capability to manage the BSM program. The Oversight Board believes that the IRS needs the following funding level for the BSM program:

- $400M in FY2002
- $450M in FY2003
- $500M+ in FY2004 and beyond

However, the IRS cannot spend over $500 million in a fiscal year effectively at its current level of management capability. All organizations involved in BSM must do a better job. Specific recommendations for key organizations are presented below.

The **IRS** must accomplish the following:

- Improve its program management ability
- Work more effectively with the PRIME Contractor
- Manage/implement change more effectively (e.g., reorganization)

The **PRIME Contractor** must accomplish the following

- Understand and achieve its responsibilities to deliver business results within budget and on schedule
- Improve its breadth and depth of skills

- Reach out to acquire the best skills available, both with the PRIME Alliance team, its subcontractors, and other unique sources of expertise

The **Administration** must do the following:

- Understand the importance and critical nature of the situation

- Understand and then support the long term plan, especially the financial investment requirements

- Hold the IRS responsible for meeting the plan

The **Congress** must accomplish the same tasks as the Administration, and, in addition, speed up the process for review and release of BSM funding.

Oversight organizations must do the following:

- Rationalize their roles to the extent possible and eliminate unnecessary overlap

- Leverage assets to advise in a more effective manner; and recognize that quality cannot be achieved by repetitious, and at times, inefficient inspection

7. Recommendations for Improving Current Operations

Notwithstanding the need for a long-term modernization program, the IRS must also improve in the short term. Potential means of realizing short-term improvements may be organizational changes, process improvements, or modifications to the legacy technology base.

Short-term organization improvements are needed to ensure that organizational modernization is working in the field. If these improvements are not realized, the foundation for future improvement in process and technology will be adversely affected. To ensure that the reorganization works, the IRS must:

- Complete the implementation of the balanced measures program
- Achieve continual learning throughout the organization
- Empower and motivate through effective communications
- Eliminate roadblocks to success

The IRS has completed its modernization reorganization with the exception of its Modernization and Information Technology Services (MITS) division, which is still in the process of implementing a structure that best serves the restructured IRS. The IRS needs to complete the restructuring of its MITS organization so that it can make the most productive use of the more than $1.6 billion invested annually in the operations and maintenance of its vast information technology environment.

Part of the funds spent by MITS is used to implement smaller modernization projects that are designed to achieve short-term improvements in processes and legacy information systems. These projects provide useful short-term improvements without waiting for larger-scale business systems modernization program. However, it is essential that these short-term projects flow logically into and integrate with the long-term solutions created through the BSM program.

The IRS is establishing and growing pre-filing activities, especially in its stakeholder and taxpayer partnership programs in its Wage & Investment (W&I) and Small Business/Self-Employed (SB/SE) divisions. As these programs are designed to reach broader segments of taxpayer, IRS needs to continuously evaluate their effectiveness. The Board believes that the IRS should be encouraged to experiment with new and innovative ways to increase taxpayer compliance through more effective communication and outreach before returns are prepared and filed. However, because there is little objective information currently available about how well such activities work, the IRS must be prepared to make meaningful assessments of these efforts and to arrive at timely decisions about their continued or expanded use.

Finally, substantive progress needs to be made in performing research on the extent and causes of non-compliance with the tax laws. The new research effort, the National Research Project, must be designed to be scientific in approach and fair to taxpayers, and the IRS must resolve quickly any issues that prevent the program from implementation.

Appendices

Appendix A — IRS Oversight Board Private Life Members' Biographies

The Oversight Board, by statute, consists of nine members, including the Secretary of the Treasury and the IRS Commissioner. Profiles of the seven private life members, who are appointed by the President and confirmed by the Senate without regard to political affiliation and solely on the basis of their professional experience and expertise, follow.

LARRY R. LEVITAN, CHAIRMAN
Retired Partner, Andersen Consulting
Larry R. Levitan retired from a 34-year career with Andersen Consulting in 1997. He held key leadership positions at the firm, which grew during his career from 500 to over 50,000 employees. Mr. Levitan became a partner in 1974 and served as managing partner of numerous Andersen Consulting operational entities. He worked with world-class clients to create business strategies, restructure organizations, management processes, and mission critical information systems. Mr. Levitan currently serves on a number of corporate boards. He received a degree in accounting from the University of Florida.

GEORGE L. FARR
Retired, Vice Chairman, American Express, Inc.
George L. Farr recently retired as the Vice Chairman of American Express, Inc., where he participated in the overall management of the company, including the strategic and operating functions. He was directly responsible for Commercial Cards, Small Business Services, Traveler's Checks, Financial Direct, and Workplace Financial Services. Prior to his service at American Express, which began in 1995, Mr. Farr was a senior partner at McKinsey and Co. in New York, where he advised domestic and international clients on a variety of management issues over a 27-year career. At McKinsey, he worked principally with consumer oriented businesses, and served at foreign posts in Switzerland and Brazil. Mr. Farr is a graduate of the University of Michigan where he received Bachelor's and Master's degrees in business.

NANCY KILLEFER
Senior Partner, McKinsey and Company
Nancy Killefer is a senior partner at McKinsey and Co., an international management consulting firm in Washington, DC, specializing in developing market strategies and improving organizational effectiveness. In 1997, President Clinton appointed Ms. Killefer as Assistant Secretary for Management/Chief Financial Officer of the Department of the Treasury. She held this post until returning to McKinsey in December 1999. At the Department of the Treasury, Ms. Killefer reported directly to the Secretary on all matters involving financial and internal management of the Department and its Bureaus - including budget, personnel, management, and procurement policies. Ms. Killefer co-chaired the Vice President's IRS Customer Service Task Force and was a major contributor to the reform and restructuring of the IRS. Ms. Killefer is a graduate of the Massachusetts Institute of Technology and Vassar College, where she received degrees in management, finance, and economics.

CHARLES L. KOLBE
Owner, Kolbe Cattle Company
Charles L. Kolbe is the Chairman of the Board of Red Oak Hereford Farms, located in Red Oak, Iowa. He is also the owner of Kolbe Cattle Company and a partner in the Midland Cattle Company. Red Oak Hereford Farms holds the exclusive contract to produce and market certified Hereford beef worldwide. Midland Cattle Company is an $80 million a-year cattle brokerage company. Mr. Kolbe is a past president of the Iowa Cattlemen's Association, past Chairman of the Iowa Beef Industry Council, and is active in many aspects of the beef industry. He is a graduate of Iowa State University.

STEVE H. NICKLES
Professor, Wake Forest University School of Law
Babcock Graduate School of Management
Steve H. Nickles is a professor of law at Wake Forest University's School of Law and Babcock Graduate School of Management in Winston-Salem, North Carolina. He is a technical advisor and consultant to the publishing industry on a wide range of issues in the areas of legal education and law proactive. At Wake Forest, Mr. Nickles has developed innovative programs for integrated, cross-disciplinary graduate studies and joint degree programs in law, banking, and business. He is a frequent guest speaker at professional education programs in the areas of bankruptcy and banking. Mr. Nickles is a graduate of the University of Arkansas and received law degrees from both the University of Arkansas and Columbia University.

ROBERT M. TOBIAS
Professor, American University
Robert M. Tobias is a professor at American University in Washington, DC, and is also the Director of the Institute of Public Policy Implementation. Mr. Tobias retired in 1999 after 31 years with the National Treasury Employees Union (NTEU), where he served as General Counsel from 1970 to 1983, and as National President from 1983 until his retirement. At NTEU, and as a member of the President's National Partnership Council, Mr. Tobias focused on establishing cooperative/collaborative labor/management relationships in the Federal government. In 1996, President Clinton appointed him to the National Commission on Restructuring the IRS. Mr. Tobias also was a member of the IRS Executive Committee. He is a graduate of the University of Michigan, where he received a degree in Business Administration, and from The George Washington University, where he received his law degree.

KAREN HASTIE WILLIAMS
Partner, Crowell & Moring
Karen Hastie Williams is a partner in the law firm of Crowell & Moring in Washington, DC, where she specializes in public contract law, legislation, and Federal budget practices. Prior to joining Crowell & Moring, she was the administrator of Federal procurement policy at the Office of Management and Budget during the Carter Administration, and also served as Chief Counsel to the Senate Committee on the Budget. Ms. Williams clerked for US Supreme Court Associate Justice Thurgood Marshall and Judge Spottswood Robinson, III at the US Court of Appeals for the District of Columbia circuit. She was the first black female to serve as a law clerk to a judge of the District of Columbia circuit. Ms. Williams is a member of several corporate boards, including SunTrust Bank-Mid-Atlantic, Gannett, Inc., Continental Airlines, Chubb Corporation, and Washington Gas Light Company. In 1994, she was Chair of the National Race for the Cure. Ms. Williams is a graduate of Bates College, the Fletcher School of Law and Diplomacy at Tufts University, and the Columbus Law School at Catholic University.

Appendix B — IRS Oversight Board 2001 Activities

The IRS Oversight Board has completed its first year of operation. During this first year the Board has engaged in a variety of activities, from organizing itself administratively to approving key IRS documents.

The Board's first meeting was held on September 13, 2000. At its first meeting, the Board elected Larry Levitan as Chairman and organized itself into the following three committees: Modernization, Performance Management, and Personnel and Organization. The Board also decided to meet approximately every two months, and conducted the following Board meetings during the year:

- November 13-14, 2000
- January 29-30, 2001
- March 20-21, 2001
- May 9, 2001
- July 30-31, 2001
- September 13, 2001
- December 4-5, 2001

All meetings were in Washington, D.C., with the exception of the November 2000 meeting that was held in Atlanta. Although the first year was a learning year for many Board members, during which the members spent numerous hours being briefed on the IRS, the Board exercised its responsibilities as enumerated in the RRA 98.

Because of the cyclic nature of the budget process, the Board spent a significant part of each meeting on one or more aspects of the IRS budget. During the reporting period, the Board reviewed and approved IRS budgets for both FY2002 and FY2003.

In approving the FY2002 budget, the Board approved a higher budget than was submitted to Congress by the Administration. Although having two budget recommendations presented an unusual situation for Congress, the Board believed the higher budget was necessary to achieve the IRS' goals for its Modernization program and reverse the decline in the number of employees at the IRS. The Board issued a separate interim report to explain why it believed the additional funds were needed by the IRS. Because the FY2003 budget is still being formulated, the Board will not comment on its budget recommendation with respect to the final Administration request.

A second area where the Board has a statutory approval responsibility is in the review and approval of IRS' strategic plans. The Board spent considerable time in reviewing the IRS Strategic Plan and approved the plan. Part of the Board's review process for both the FY2002 budget and the IRS Strategic Plan was to conduct a public meeting and obtain input from IRS external stakeholders on their comments on both IRS' budgetary needs and its Strategic Plan.

The Board also invested time in several other topics of strategic importance. The IRS Business System Modernization program was on the agenda at virtually every Board meeting. Other topics of note included personnel and organization issues associated with IRS organization modernization program, performance measures in use at the IRS, especially the Balanced Measures program, the need for compliance research, filing season status, the Mellon Bank lockbox situation, the selection process for the National Taxpayer Advocate and Deputy Commissioner for Modernization, and a review of IRS' senior executive evaluation and compensation.

The three committees of the Board also met periodically in person or by telephone. The Modernization Committee met several times to review in-depth progress of the IRS' Business Systems Modernization program, including such topics as management capability, schedule progress, and needed improvements to the program.

The Performance Management Committee met several times during the year to review IRS progress in rolling out its Balanced Measures program, examine specific performance issues associated with the measurement of quality of service at IRS Taxpayer Assistance Centers (walk-in sites), and most importantly, reviewed the plans of all four Business Operating Divisions to use collected performance measures data to develop and implement plans to improve performance over the coming year.

In keeping with the Board's statutory responsibility to review the selection, evaluation, and compensation of senior IRS executives, the Committee on Personnel and Organization conducted a thorough review of the performance evaluations and proposed bonuses of 13 top IRS executives. This action will be followed up in the upcoming year by a Board review of the FY2002 commitments of these executives as well as a review of their performance at year end. The committee also interviewed Nina Olson prior to her selection as National Taxpayer Advocate.

Administratively, the Board acquired office space and hired a Staff Director, who will be responsible for hiring a small number of additional staff that will assist the Board in carrying out its mission.

In keeping with the RRA 98 requirement to report Board travel expenses to Congress, the Board incurred $39,622 in travel expenses for Board members and staff in FY2001, primarily for travel to and from board and board committee meetings.

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